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15 *Attorneys for Mortgages Ltd. 401(k) Plan*

16 **IN THE UNITED STATES BANKRUPTCY COURT**
17 **FOR THE DISTRICT OF ARIZONA**

18 In re:) In Proceedings Under Chapter 11
19 MORTGAGES LTD.,)
20 an Arizona corporation,) Case No. 2:08-bk-07465-RJH
21)
22) **401(K) PLAN'S REPLY TO**
23) **LIQUIDATING TRUSTEE'S OBJECTION**
24) **TO 401(K) PLAN'S MOTION TO RATIFY**
25) **401(K) PLAN APPOINTMENTS AND**
26) **DEFINE THE LIQUIDATING**
27) **TRUSTEE'S ROLE WITH RESPECT TO**
28) **THE 401(k) PLAN**

29 **I. The Duly Appointed Trustees Have The Only Legal Right To Serve As Plan Fiduciaries**

30 The 401(k) Plan ("Plan") filed a Motion seeking to ratify the appointment of Chris Olson and
31 Ryan Walter as co-trustees of the Plan. These men were appointed pursuant to the authority vested in
32 the Plan under applicable ERISA law. ERISA is crystal clear that the only individual(s) or entity
33 who has responsibility for the assets of an ERISA employee benefit plan is the Plan trustee(s). As
34 such, one of the key responsibilities of an ERISA trustee, when a plan has been terminated, is to

1 marshal the Plan's assets and distribute those assets to participants. This responsibility, however, lies
2 solely with the ERISA plan trustee(s) -- not the company who has sponsored the plan, not a Chapter
3 11 debtor, and most certainly, not a liquidating trustee for that debtor's estate. Nonetheless, issues
4 have arisen in the present case that require some assistance of the Court to determine the proper party
5 or parties to serve in that role.
6

7 Objections have been filed by Robert Furst, a Plan participant, to the continuation of Mr.
8 Olson and Mr. Walters in that role. In addition, the Liquidating Trustee has objected, claiming that
9 he has heard expressions of concern by certain Plan participants. Of course, not all the Plan
10 participants have objected to these men serving. In fact, Ann Flaherty, who holds one of the largest
11 shares in the Plan, has indicated her support of Mr. Olson and Mr. Walter. *See Attached Exhibit A,*
12 *September 15, 2009, Letter to Judge Haynes.* Ms. Flaherty is only one of many Plan participants who
13 have expressed support for Messers. Olson and Walters.
14

15 The Liquidating Trustee asserts concerns over alleged actions and inactions by Mr. Olson, and
16 asserts concerns regarding Mr. Walter's qualifications. The Liquidating Trustee further asserts that
17 these participant objections led him to freeze the Plan's accounts, and seize the books and records.
18 While the Liquidating Trustee may be acting out of a desire to protect the Plan participants, these
19 actions are both misguided and prohibited under ERISA.
20

21 The Liquidating Trustee's refusal to allow the Trustees to administer the assets of the Plan is
22 causing actual damages to the Plan. As an example, one of the homes in which the Plan has an
23 undivided interest was robbed over two months ago. It has taken the involvement of Mr. Jenkins to
24 move the Liquidating Trustee to provide the required information (in the Liquidating Trustee's
25 possession) to allow the insurance claim to proceed. In addition, there have been problems with such
26 routine matters as paying utility bills for the properties owned by the Plan. Furthermore, the Plan
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1 understands that decisions are being made with regard to certain Plan assets, specifically those that
2 are jointly held with members of the ML Manager Board, without the input of the Plan. See Exhibit
3 B, September 15, 2009 email from Chris Olson to ML Manager LLC Board. What has become clear
4 over the last few months, since the Liquidating Trustee “froze” the Plan, is that doing nothing is
5 causing harm to the Plan, and by extension the Plan participants.
6

7 The Plan seeks an Order of the Court directing the Liquidating Trustee to immediately turn
8 over the books and records to the Trustees of the Plan. These Trustees must be allowed to administer
9 the Plan, manage its assets and prevent further damage to those assets. To the extent that Mr. Olson
10 is believed to be an impediment to this benefit to the Plan, he has indicated that he would be willing
11 to step aside in favor of Mr. Walter. In addition, another Plan participant has come forward to share
12 the work of administering the Plan. The Plan requests the Court make these appointments at the
13 hearing on September 17, 2009. To the extent the participants wish to challenge the qualifications of
14 these Trustees, or to seek additional parties to serve in a fiduciary capacity, the Plan proposes the
15 Court schedule an evidentiary hearing within 45 days to address such concerns.
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19 **II. ML Servicing Co., Inc. has a conflict of interest and has no authority over the 401(k)**
20 **Plan under the Plan of Reorganization.**

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22 1. Liquidating Trustee has a Conflict of Interest.

23 While the Liquidating Trustee’s concern in his Objection for the well-being of the 401(k) Plan
24 and its participants is laudable, that concern is both perplexing and a source of consternation to the
25 Plan Trustees and to many Plan participants. This consternation is based on the simple fact that the
26 Liquidating Trustee has a direct conflict of interest as to his concern for the Plan and as to his
27 fiduciary duties to the Liquidating Trust. This conflict is illustrated by two uncontroverted facts.
28

1 First, both the 401(k) Plan and a number of Plan participants are listed as potential “targets” on the
2 Liquidating Trustee’s “target list” (see Exhibit E to the Official Committee of Investors’ Disclosure
3 Statement).

4 Second, and as stated by the Liquidating Trustee in his Objection to Haynes Benefits PC’s
5 Application for Allowance of Administrative Claim, certain liability insurance policies were
6 purchased by Mortgages Ltd. which may provide a source of recovery for Plan participants (for
7 potential breaches of fiduciary duty). Those policies, however, are also a potential source of recovery
8 for other creditors of Mortgages Ltd. The fact that the policies are now controlled by the Liquidating
9 Trustee, combined with the fact that both the Plan participants and Mortgages Ltd.’s creditors view
10 the policies as a potential source of recovery, further illustrates the Liquidating Trustee’s conflict.
11

12 Without question, the Liquidating Trustee has a fiduciary responsibility to the creditors of
13 Mortgages Ltd. When the 401(k) Plan and its participants have been listed as a “target” of those
14 creditors, the Liquidating Trustee cannot now assert his actions have been “designed to protect the
15 participant’s interests.” (See Liquidating Trustee’s Objection at p.2). He cannot serve two masters –
16 the creditors and an ERISA entity whose assets are held in trust for the benefit of former employees
17 who may be targets of those creditors and who may be seeking access to the same assets (vis a vis,
18 the liability insurance policies). Interestingly, and by placing a “freeze” on the 401(k)’s accounts, the
19 Liquidating Trustee may have already become a 401(k) Plan fiduciary (albeit, unintentionally). It is
20 paramount, however, that he not be permitted to continue in this conflicted role any further.
21

22
23 2. The Amended Plan of Reorganization does not transfer authority over the 401(k) Plan
24 to the Liquidating Trustee.
25

26 The Amended Plan of Reorganization states that the Liquidating Trust shall be “created and
27 administered solely to implement the Plan [of Reorganization].” See Section 6.2. In this respect, the
28

1 Liquidating Trustee is to be a representative of the Estate “**appointed for the purposes of, among**
2 **other things, pursuing the Avoidance Actions and Causes of Action on behalf of the Debtor’s**
3 **Estate.** In furtherance of that objective, the Liquidating Trustee shall have the rights of a Trustee
4 appointed under the Bankruptcy Code §1106 *as it relates to the Non-Loan Assets.*”

5
6 Similarly, the ML Liquidating Trust Agreement provides in Section 13b that the Liquidating
7 Trustee shall be “**restricted to the holding, collection, conservation, protection and administration of**
8 **the Liquidating Trust Estate ... and the payment and distribution of amounts as set forth herein for**
9 **the purposes set forth in this Agreement.**” The Trust Agreement, therefore, is very clear that the sole
10 goal of the Liquidating Trustee is to collect and preserve Estate assets and distribute those assets to
11 the beneficiaries as provided for under the Trust Agreement.

12
13 The “Liquidating Trust Estate” is defined to mean **the assets to be transferred to the**
14 **Liquidating Trust pursuant to the Plan [of Reorganization].”**

15 The “Non-Loan Assets” that are being transferred to the Liquidating Trust include only the
16 following:

17
18 **Non-Loan Assets** means and includes all assets that are not used to make those
19 payments that are due on the Effective Date of the Plan, and that are not
20 transferred to one of the ML Manager LLC or the Loan LLCs on the Effective
21 Date of the Plan. **Non-Loan Assets** shall specifically include all of the
22 Debtor’s interest in real property; avoidance and third-party claims; Avoidance
23 Actions and Causes of Action; tangible assets, including, without limitation,
24 computers, intellectual property, furniture, fixtures and equipment; and
employee and related business contracts and customer lists, excluding existing
servicing rights or agency agreements, related to the ML Loans, and excluding
the Debtor’s rights, if any, to interest spread, fees, extension fees, default
interest and other interest, fees and charges arising out of or related to the ML
Loans or the servicing rights or agency agreements.

25 This definition does not include the 401(k) Plan, nor the assets of the 401(k) Plan. As such,
26 the Liquidating Trustee has no authority over the 401(k) Plan. His actions to freeze Plan accounts,
27 therefore, were not only improper but have damaged the 401(k) Plan and cannot be permitted to
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1 continue. Authority over the 401(k) Plan must, therefore, be immediately vested in the trustees who
2 were properly appointed by the Debtor, until those individuals resign or are otherwise properly
3 removed from office.

4 3. The Disclosure Statement is clear that 401(k) Plan is to act at the direction of its
5 Trustees.
6

7 In its Amended Disclosure Statement, the Official Committee of Investors states:

8 The Loans in which the Mortgages Ltd. 401(k) Plan holds the ownership
9 interest will not be transferred to Loan LLCs. Instead **the Trustee(s) of the**
10 **Mortgages Ltd. 401(k) Plan shall make their own decisions and decide**
11 **who will service their loans.**

12 Disclosure Statement, II.D., fn. 1, p. 7 (*emphasis added*).

13 This statement could not be more clear—the 401(k) Plan Trustees, not the Liquidating Trustee
14 or any other person or entity, are the only individuals who may make decisions with respect to the
15 Plan and the mortgage loans held by the Plan.

16 **III. Trustees are qualified to serve and supported by a majority of the Participants.**

17 The two trustees, Chris Olson and Ryan Walter, are qualified to serve and, as stated above,
18 are supported by a majority of participants. As stated in the Motion, Mr. Olson served as the
19 Debtor's chief operating officer and a co-trustee of the Plan for many years. Mr. Walter, on the other
20 hand, was engaged by the Debtor as an outside ERISA consultant in 2001 to devise the platform for
21 the Plan. Walter had extensive experience designing ERISA plans and was also a registered
22 investment advisor.
23

24 Both trustees are substantial participants in the Plan and have a vested interest in the
25 preservation and recovery of Plan assets. Both trustees were integrally involved in the Debtor's
26 business. In this regard, they understand the Phoenix real estate market, mortgage loans, the
27 servicing of those loans and the collection (or, if necessary, foreclosure) of such loans.
28

1 The trustees believe they have substantial support from Plan participants. The trustees have
2 no inherent objection to the engagement of an independent fiduciary, but believe (1) that the Plan will
3 be better served (and at a lesser cost to the Participants) if it is managed by Plan participants, and (2)
4 that any fiduciary, if ultimately selected, must truly be independent and serve jointly with the existing
5 trustees.
6

7 **IV. James Cordello, former Plan trustee, has agreed to serve as a third Plan trustee.**

8 James Cordello, who is also a former employee of the Debtor, has agreed to serve as a third
9 trustee to the Plan. Mr. Cordello actually selected Mr. Walter as the consultant to design the 401(k)
10 Plan, and Mr. Cordello served as a Plan trustee for nearly 5 years. Similar to Messrs. Olson and
11 Walter, Mr. Cordello understands not only the Plan, but also understands the Phoenix real estate
12 market and mortgage loans. He also has a significant account balance in the Plan and has a
13 significant interest in preserving that account.
14

15 **V. Conclusion**

16 The 401(k) Plan respectfully requests that its Motion be approved. If the Court determines
17 that it is in the best interest of the Plan participants that an evidentiary hearing occur to determine
18 whether Messrs. Olson, Walter and Cordello should serve as trustees, the Plan requests that
19 immediate control and authority over the Plan be vested in trustees Olson and Walter pending that
20 hearing. At this point, the Plan is being damaged daily. Loan workouts have been, and continue to
21 be, delayed; the Plan has not been permitted to participate in negotiations with respect to mortgage
22 loans in which the Plan shares an interest with non-Plan investors; and damage has occurred to real
23 estate owned by the Plan due to the Liquidating Trustee's freezing of the Plan's accounts. The Plan
24 cannot be permitted to remain adrift, but instead, control of the Plan must be vested in the Plan
25 trustees in order that they can take immediate and unfettered actions to preserve the Plan's assets.
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RESPECTFULLY SUBMITTED this 16th day of September, 2009.

/s/ Robert A. West
Haynes Benefits PC, Attorneys at Law
Robert A. West

/s/ Thomas S. Moring
Thomas S. Moring

Exhibit A

ANN FLAHERTY

908 E. KEIM DRIVE
PHOENIX, AZ 85014
PHONE: 602-277-2512

EMAIL: PHANNF@YAHOO.COM

September 15, 2009

Dear Judge Haynes:

I am writing this letter to urge you to appoint Christopher Olson, Ryan Walter and James Cordello as Trustees of the Mortgages Ltd. 401(k) Plan. They are good men, and will administer the plan with the best interests of all the participants and for the least cost of any of the other proposed plans. They have been employees of Mortgages Ltd., and know the loans and the borrowers. I trust them to make the best decisions for all concerned.

I was an employee of Mortgages Ltd. for 24 years, and was laid off in June 2008 after Scott's suicide and bankruptcy of Mortgages Ltd. I can tell you that everyone who was in the plan was ecstatic over the great returns quarter after quarter. This was because all the investments were in Mortgages Ltd. Loans. The employees voted to do this, and anyone who entered the plan after that vote signed a form stating that they understood that all investments were in Mortgages Ltd. loans.

No one was ever coerced to join the plan, or roll over funds from a previous employer, and could cease making contributions at any time.

I believe there is a personal attack being made on Chris Olson, the current Trustee. Mortgages Ltd. was run as a dictatorship by Scott Coles, and no one, no matter what their title, had any real influence on his decisions. You did it Scott's way or you could leave. But no one did, largely because of the wonderful way the 401(K) Plan grew. Chris did his best in this situation, but in reality had not much control.

My concern that is any of these other third-party trustees would have no concern about me and what's best for me. They would be tempted to liquidate the plan as soon as possible, when it might be prudent to buy some time and see if the values come back some.

Thank you for allowing me to express my opinion. I hope it has some influence, because I truly believe in these men and their capabilities and feel they are being treated badly.

Sincerely,

Exhibit B

Tom

From: Rachel Schwartz and Chris Olson [cosmoaz@earthlink.net]
Sent: Tuesday, September 15, 2009 10:34 PM
To: ML Manager LLC Board; bbuckley@cox.net; bill@pentadholdings.com;
Scott.Summers@nbarizona.com; pollack@edpco.com
Cc: Ryan Walter; Bob West; Tom Moring
Subject: GP Carefree Cave Creek Trustee Sale
Mark Winkelman and ML Manager board,

I am very concerned by the lack of cooperation that you are exhibiting towards the Mortgages Ltd. 401k Plan. Once again, you have made decisions regarding the trustees sale for the GP Properties Carefree Cave Creek loan without consulting myself or Ryan Walter, the co-trustees of the Mortgages Ltd. 401k plan, which is an approx. 46% stakeholder in this loan. Per my discussion with Chris McNichol of Gust Rosenfeld, you have again moved the trustee sale (to September 23, 2009) without even the slightest attempt to consult with us. This is unacceptable behavior.

Mark, you had indicated to Ryan and I at a lunch meeting at BJ's restaurant on or about August 21st or 28th that you would work cooperatively with the 401k Plan on assets which were co-owned by the 401k Plan and investors at Mortgages Ltd. (or the LLC for this loan managed by ML Manager) and that you would keep us informed of actions that the ML Manager was taking in regards to these assets. That has yet to happen. I contacted you the week of August 31 and told you that we **MUST** be included in these decisions regarding co-owned assets. That request has apparently been ignored.

We have been asking to be included in your agenda for the ML Manager boards weekly Tuesday meetings since early August to no avail. I hope that you reverse your current position and decide to include us in your decisions or we will take the appropriate action necessary to protect the Mortgages Ltd. 401k plan interests.

Thank you.

Chris Olson
Mortgages Ltd. 401k Plan Co-Trustee

9/16/2009

CERTIFICATE OF SERVICE

I hereby certify that on September 16, 2009, I electronically transmitted the attached document to the Clerk's Office using the CM/ECF System for filing and transmittal of a Notice of Electronic Filing to the parties in interest via the Court's ECF System and to the following, whose registration status is unknown:

<p>Kevin J. Blakley Gammage & Burnham, P.L.C. Two North Central Avenue, 18th F1 Phoenix, AZ 85004 Kblakley@gblaw.com Attorney for: Ronald L. Kohner</p>	<p>Charles A. Lamar Justin C. Lamar 818 North First Street Phoenix, AZ 85004 clamar@kmldevelopment.com jlamar@kmldevelopment.com Attorney for: University & Ash; Roosevelt Gateway, Roosevelt Gateway II and KML</p>	<p>Ryan W. Anderson Guttilla Murphy Anderson, PC 4150 West Northern Avenue Phoenix, AZ 85051 randerson@gamlaw.com Attorney for: Department of Financial Institutions</p>
<p>Jerome K. Elwell Warner Angle 3550 N. Central, #1500 Phoenix, AZ 85012 jelwell@warnerangle.com Attorney for: Francine Haraway</p>	<p>Felecia A. Rotellini Robert Charlton AZ Dept. of Financial Institutions 2910 N. 44th St., Suite 310 Phoenix, AZ 85018 Rotellini@azdfi.gov rcharlton@azdfi.gov</p>	<p>C. Bradley Vynalek Quarles & Brady LLP One Renaissance Square 2 North Central Avenue Phoenix, AZ 85004 bvynalek@quarles.com Attorney for: Ashley Coles</p>
<p>Scott A. Rose Kerry M. Griggs The Cavanaugh Law Firm 1850 N. Central Ave., #2400 Phoenix, AZ 85004 srose@cavanaghlaw.com kgriggs@cavanaghlaw.com Attorney for: Central PHX Partners</p>	<p>Robert J. Spurlock Bonnett, Fairbourn, Friedman & Balint 2901 N. Central Avenue, #1000 Phoenix, AZ 85012-3311 bspurlock@bffb.com Attorney for: Foothills Plaza IV, LLC</p>	<p>Sheldon Sternberg 3212 Rainbow Ridge Drive Prescott, AZ 86303 sheldonsternberg@q.com Pro Per</p>
<p>Patrick R. Barrowclough Atkinson, Hamill & Barrowclough PC 3550 N. Central Ave., #1150 Phoenix, AZ 85012 Patrick.Barrowclough@azbar.org Attorney for: Chuck Niday, Trustee for Ross Verne Family</p>	<p>Kelly Haddad 21586 N. Greenway Road Maricopa, AZ 85238 (520) 251-7303 Kellyhaddad01@mac.com Kelly Haddad and Navval Haddad, Creditors – Pro Per</p>	<p>Robert Furst rgfurst@aol.com</p>

By: /s/ Thomas S. Moring